Original

DOCKET FILE COPY ORIGINAL

Before the
Federal Communications Commission
Washington, D.C. 20554

In the Matter of	)	
	)	
Regulatory Treatment of LEC Provision of Interexchange Service Originating in the LEC's Local Exchange Area	)))	CC Docket No. 96-149
	)	
and	)	
	)	
Policy and Rules Concerning the Interstate, Interexchange Marketplace	))	CC Docket No. 96-61

REPLY OF ALLTEL COMMUNICATIONS, INC. TO OPPOSITIONS TO PETITIONS FOR RECONSIDERATION

ALLTEL Communications, Inc., ("ALLTEL") hereby respectfully replies to the various petitions filed in opposition to its petition seeking reconsideration of the Order[1] in the above-captioned proceeding. In support thereof, the following is respectfully set forth.

ALLTEL, as well as other small and medium sized LECs sought reconsideration of the Order because, in their judgment, the Commission had failed to adequately justify the continued imposition of safeguards and differentiate these companies from the larger regional local exchange companies (and the anticompetitive potential those larger companies pose in the interstate, interexchange market) based upon a number of

[1] Second Report and Order in CC Docket No. 96-149 and Third Report and Order in CC Docket No. 96-61, FCC 97-142 (released April 18, 1997) (the" Order").

simple and readily discernible facts. Among those facts were: the absence of contiguous multistate local exchange territories; the LECs' lack of end-to-end interexchange facilities; the LECs' provision of interstate, interexchange service through resale; the sufficiency of the Part 64 accounting rules; the regulatory oversight of the interstate access tariff regime; and the absence of either any abuse or further evidence that the Fifth Competitive Carrier[2] safeguards remain necessary.

Those opposing the petitions for reconsideration, however, refuse to acknowledge these clear differences in status of the small and midsized companies and the equally clear implications for their lack of adverse competitive impact in the interstate, interexchange market. The oppositions insist instead on lumping the entire local exchange industry into a single large monolith purportedly bent on chasing from the marketplace the very companies upon whose facilities the small and midsize LECs rely for the provision of wholesale and retail long distance services. Rather than base their response in concrete examples which directly reflect the size, scope and resources of small and midsize LECs, certain opponents embark upon a course of speculation and misapplication of economic theory, ultimately failing to point to any violation by one of the companies seeking reconsideration.

For example, in addressing the adequacy of the Part 64 rules, MCI[3] makes immaterial references to the misdeeds of the Bell Operating Companies and GTE,

---

[2] Policy and Rules Concerning Rates for Competitive Carrier Services and Facilities Authorizations Therefor, Fifth Report and Order, CC Docket No. 79-252, 98 FCC 2d 1191 (1984) ("Fifth Competitive Carrier")

[3] See MCI opposition at page 7.

companies which present a totally different set of circumstances to the Commission because their size and scope decidedly differs from those of small and midsize LECs. In the last analysis, however, neither these small and midsize companies nor their local exchange markets are of sufficient size to provide the economic incentive to leverage their local bottlenecks and engage in the anticompetitive behavior complained of in the oppositions. Indeed, given the characteristics of these companies seeking reconsideration, it is highly unlikely that these companies have the ability to corrupt the long distance market even assuming, for the sake of argument, that these companies blatantly disregarded the law.[4]

I. The Implications of the 1996 Act.

MCI argues that nothing in Section 272 of the Act implies that the Commission should not impose safeguards on an independent LEC providing interexchange service. MCI cites section 601(c)(1) of the 1996 Act for the proposition that the Commission is not to presume that any regulation has been superseded by Congress unless expressly so provided.[5] This is largely a straw argument inasmuch as nothing in the 1996 Act requires the continuation of the separations or Fifth Competitive Carrier safeguards. ALLTEL argued, and MCI does not refute, that it is the Commission which is under the continued obligation to justify its regulation and to forego regulation where it is

[4] In this connection, ALLTEL notes that the Spulber statement attached to the Comments of USTA filed on August 29, 1996 in this proceeding provided substantive analysis of the lack of incentive for independent LECs to engage in the very activities complained of by AT&T and MCI. See attached pages of Statement of Daniel F. Spulber at pages 22-58.

[5] MCI opposition at pages 4-6.

either no longer necessary or otherwise unjustified on the record.[6] This approach is in keeping with the forbearance provisions in Title IV of the 1996 Act and the general notion that its provisions were to be construed in a deregulatory manner.

The absence of any reference to the small and midsize companies in section 272 and fair reading of the provisions of the 1996 Act, moreover, exhibits the themes expressed in the letter of the Members of Congress.[7] As noted in the ALLTEL and USTA filings, what is clear is that the Congress considered the extent to which the long distance market required the protections afforded by safeguards and separation requirements. Congress chose to place those requirements only on the Bell Operating Companies and by clear implication, the Commission is free to remove the safeguard requirements from other LECs. Section 272, which addresses long distance safeguards, is on its face exclusively limited in its application to the Bell Operating Companies and neither expands or contracts the Commission's authority or obligation to remove outmoded safeguards when and where appropriate. MCI's attempt to "drive the point home" by reference to section 272(f)(3) therefore fails.[8] Clearly, the import of Section 272(f)(3) when construed within the context of the 1996 Act is limited to the Commission's authority to either extend the statutory safeguards placed on the BOCs

---

[6] See ALLTEL Petition for Reconsideration at page 2.

[7] Letter dated June 25, 1997 to the Honorable Reed E. Hundt from U.S. Representatives Tauzin, Oxley, Boucher, Dingell et.al. The letter, which counts among its signatories the ranking member of the full committee and the chairman of the subcommittee, is downplayed by MCI as an "after-the-fact" expression of intent which hardly qualifies as any indication of Congress' thinking on the matter. It goes without saying, however, that the signatories to the letter were slightly closer to the process than MCI.

[8] ALLTEL does note, however, that it is somewhat quizzical for MCI to argue on the one hand that the absence of any reference to independent LECs in Section 272 is of no import, while on the other, citing to the same section in attempting to bootstrap its argument.

after the three year period or to place less onerous (i.e. Fifth Competitive Carrier safeguards) on the BOCs after the three year period elapses.

II. Part 64 of the Rules and the Need for Separations.

MCI charges that misallocation remains a problem particularly for rate of return LECs which, in MCI's view, are in the same situation they were in when the Fifth Competitive Carrier safeguards went into effect. MCI goes on to bemoan allegedly "widespread cost misallocations and cross subsidies by the BOCs and GTE" and the Commission's "limp" enforcement.[9] Here again the best and most concrete example that MCI can muster to illustrate its point is a reference to the BOCs and not to the small or midsize companies seeking reconsideration.

The Geppert affidavit attached to the USTA petition for reconsideration exactingly detailed the operation and sufficiency of the Commission's Part 64 accounting rules. These matters are unrefuted by the MCI opposition. The Geppert affidavit exhaustively illustrates the manner in which costs are allocated and separated between jurisdictions and between competitive and non-competitive services. No persuasive argument or example directly applicable to small and midsize LECs has been proffered to demonstrate that the Part 64 rules are anything but effective in policing misallocation and cost shifting by these companies. Indeed, the very example cited by MCI as a failure of the rules is, in fact, proof the rules are effective in ferreting out the very misallocation with which MCI is so concerned.

---

[9] MCI opposition at pages 6-8.

Apparently nothing has changed since 1984 in MCI's world -- not the 1996 Act, its elimination of the barriers to entry, the availability of unbundled network elements, or the emergence of huge long distance competitors no longer in need of the Commission's regulatory largesse. While MCI continues to point accusingly at the local exchange bottleneck as the competitive culprit, it fails to acknowledge that small and midsize LECs' bottlenecks are subject to erosion and are generally not of sufficient size to provide either the power or the incentive to leverage into the long distance market.[10]

III. The Implications of Resale.

MCI attacks the resale argument, alleging that most ILECs only purchase interexchange transport and provide their own access services. Having set up the argument, MCI once again raises the specter of the small and midsize LECs' incentive to misallocate costs and engage in prices squeezes by failing to impute the cost of access in their interexchange offerings and otherwise discriminate in favor of their long distance service. As noted in Dr. Spulber's statement[11], the failure by a small or midsize LEC to impute access charges in its resold long distance offerings produces an uneconomic and undesired result: it reduces the LEC's profit. Indeed, pricing interexchange service below cost is an activity which can only be economically viable in the long term as part of a predatory pricing scheme, the intent of which is to drive the IXCs, upon which the small and independent LECs rely, out of the wholesale and

---

[10] See attached pages of the Spulber statement at pages 32-40.

[11] See attached pages of the Spulber statement at pages 40-48.

retail market entirely in the hopes that lost profits can be made up at a later date. Inasmuch as they are generally without their own interLATA facilities and require interLATA transmission capability, driving IXCs out of the wholesale market is not a desired result.

ALLTEL buys end-to-end interexchange service which it generally sells at rates approximately 10% below AT&T's MTS rates. The opponents allege that, even where independent LECs are pure resellers of end-to-end interexchange service, the independent LECs may still engage in a price squeeze by pricing their retail interexchange offering below cost.[12] Again, MCI's reasoning produces the uneconomic result of a sacrifice in profits without any countervailing benefit to the small or midsized LEC. There is simply no incentive for a small or midsized LEC to engage in this type of behavior, nor is there any indication that the Part 64 accounting procedures would be less than effective in exposing it should it occur. To the extent that MCI complains of the small and midsize LEC's ability to provide subscribers with a lower retail rate,[13] it challenges the underlying economics and public benefits of the resale market generally. So long as the LEC is not selling end-to-end minutes at a price below wholesale cost, there is nothing inherently anticompetitive about an independent LEC buying bulk minutes at wholesale and reselling them at a price lower than that offered by the underlying IXC's retail rate. Rather, this result occurs simply through

---

[12] See AT&T opposition at page 7; MCI opposition at page 12.

[13] See MCI opposition at page 12.

bulk resale placing downward pressure on retail rates, a result which the Commission has on numerous occasions found to be in the public interest.

Lastly, as noted by USTA, the IXC's are now free to construct their own facilities, deal with a competitive access provider or purchase unbundled network elements in order by pass access charges or, at a minimum, subject access rates to downward pressure. In ALLTEL's view, retention of the safeguards are not justified simply because an IXC refuses to take advantage of the new opportunities provided under the 1996 Act.

IV. Independent LECs With Less Than Two Percent of the Nation's Access Lines Cannot Inflict Competitive Injury on the Giants of the Interexchange Business.

MCI attacks ALLTEL's suggestion that companies with less than two percent of the nation's access lines should be relieved from the Fifth Competitive Carrier safeguards claiming that these companies can inflict competitive injury and have, in fact, done so. As evidence of this injurious conduct, MCI points only to SNET, the largest of the so-called two percent companies, and claims, as its prime example of anticompetitive conduct, a PIC freeze. SNET also, according to MCI, is a two percent company with significant interexchange operations.[14]

There is nothing inherently anticompetitive about a PIC freeze when entered at the behest of a subscriber. Indeed, PIC freezes may be the most effective way in which a subscriber may protect themselves from "slamming", a practice with which certain IXC's are intimately familiar. While MCI sees nothing magical about the two

[14] See MCI opposition at pages 14-16.

percent criterion, it does, in fact, capture a group of small and midsize LECs with unique characteristics, not the least of which is the general absence of facilities which cross state boundaries. It therefore is worthy of note that although SNET may have interexchange facilities, they are intrastate[15] in nature and beyond the scope of this proceeding inasmuch as it is the interstate, interexchange market which is subject to the Commission's jurisdiction. As noted in ALLTEL's petition, the two percent criterion separates those local exchange carriers whose scope and size require regulation, from those that do not. SNET, the largest of the two percent companies, operates in a substantially competitive environment with over 26 carriers certified to provide local service in its territory.[16] SNET is incapable of driving the IXCs from the market inasmuch as it would run out of cash far sooner than MCI, AT&T or WorldCom were it to engage in a predatory pricing scheme. MCI has offered no substantiation as to why the two percent companies are a competitive threat other than to restate its

---

[15] See Comments of the Independent Telephone and Telecommunications Alliance at pages 10-11.

[16] Id.

allegations of price squeezes and misallocation dealt with above. Such arguments should be rejected.

Respectfully submitted,

ALLTEL Communications, Inc.

By: ____________________

Glenn S. Rabin
Federal Regulatory Counsel

ALLTEL Corporate Services, Inc.
655 15th Street, N.W.
Suite 220
Washington, D.C. 20005
(202) 783-3976

Dated: September 23, 1997

Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C. 20554

In the Matter of	)	
	)	
Implementation of the Non-Accounting Safeguards of Sections 271 and 272 of the Communications Act of 1934, as amended;	)))	CC Docket No. 96-149
	))	
and	)	
	)	
Regulatory Treatment of LEC Provision of Interexchange Services Originating in the LEC's Local Exchange Area	)))	

Statement of Daniel F. Spulber
Northwestern University

My name is Daniel F. Spulber. I am the Thomas G. Ayers Professor of Energy Resource Management and Professor of Management Strategy at the J.L. Kellogg Graduate School of Management, Northwestern University, where I have taught since July, 1990. I received my B.A. in Economics from the University of Michigan, and my M.A. and Ph.D. in Economics from Northwestern University. Before joining the faculty of Northwestern University, I was Professor of Economics and Professor of Economics and Law at the University of Southern California. I have also taught economics at Brown University and the California Institute of Technology.

I have been ranked 6th in the United States in the listing of top 50 economists by pages published in leading journals, 1984-1993, "Trends in Rankings of Economics Departments in the U.S.: An Update, Loren C. Scott and Peter M. Mitias, *Economic Inquiry*, v. XXXIV, April, 1996, pp. 378-400.

I have conducted extensive research over the last eighteen years in the areas of regulation, industrial organization, microeconomic theory, and energy economics. In my scholarly research and consulting work, I have studied issues of regulation and competition in network industries, including telecommunications. I am the author of author of *Protecting Competition from the Postal Monopoly*, with J. Gregory Sidak, published in 1996 by the American Enterprise Institute, *Regulation and Markets* published in 1989 by M.I.T. Press, and coeditor of *Essays in the Economics of Renewable Resources*, with Leonard J. Mirman, published in 1982 by Elsevier-North Holland. I have published over 50 articles on regulation, pricing and related topics in numerous academic journals, including the *Yale Journal on Regulation*, the *New York University Law Review*, the *Journal of Economic Theory*, the *Quarterly Journal of Economics*, the *Rand Journal of Economics*, *The Review of Economic Studies*, and the *American Economic Review.* I am the founding editor of the *Journal of Economics & Management Strategy*, published by MIT Press.

I have been asked by the United States Telephone Association to conduct an economic analysis concerning independent local exchange carrier ("LEC") issues pertaining to the question of whether or not the independent LECs should be considered non-dominant in offering interLATA telecommunications services and pertaining to the structural separation safeguards applied to these companies by the Federal Communications Commission (FCC). In my statement, I respond to some of the questions posed in the FCC's NPRM (CC Docket No. 96-149).

Based on my economic analysis, my conclusions are as follows:

(1) The independent LECs should not be classified as dominant carriers in offering interstate, domestic, interexchange telecommunications services (hereafter interexchange services).

(2) The protections afforded by the separate affiliate safeguards are rendered unnecessary by competition in interexchange services and in the local exchange. Moreover, the protections themselves serve as competition-reducing entry barriers and therefore should be eliminated.

My statement is outlined as follows. In Section I, I begin by examining the question of whether or not the market power of the independent LECs supports elimination of "separate affiliate" safeguards and classification of independent LECs as non-dominant carriers. I show that the relevant product market is interstate, domestic, interexchange telecommunications service and the relevant geographic market is national in scope. I further consider the independent LEC's market share in interexchange telecommunications, the demand and supply elasticities in interexchange telecommunications, and the cost structure, size and resources of the independent LECs. In Section II, I consider the impact of competition in the local exchange to determine whether or not the independent LECs have the opportunity or the incentive to leverage market power through "raising rivals' costs" or cross subsidization of interexchange telecommunication. I emphasize that local exchange telecommunications no longer is a natural monopoly and that barriers to entry into local telecommunications have fallen or been significantly reduced. I show that the independent LECs have no economic incentive or opportunity to engage in monopoly leveraging, "raising rivals' costs," or cross subsidization. Finally, in Section III, I explain why the separation and dominant-carrier regulations create barriers to entry into interexchange telecommunications, thereby impeding competition, particularly because they are asymmetrically applied.

I. Economic Analysis of Telecommunications Markets Supports Elimination of "Separate Affiliate" Safeguards and Classification of Independent LECs as Non-Dominant Carriers

The Commission defines "dominance" as having market power. Market power is said to arise when a firm is able profitably to raise its price substantially above the competitive level, or to raise market prices by restricting their output.[1] The Commission's Fourth Report and Order cites the Areeda and Turner definition of market power as "the ability to raise prices by restricting output" and the Landes and Posner definition of market power as "the ability to raise and maintain prices above the competitive level without driving away so many customers as to make the increase unprofitable."[2] By these, or any other reasonable definition, the market power of the independent LECs in interexchange telecommunications is negligible. Therefore, the independent LECs should not be classified as dominant carriers in interexchange telecommunications. In the next section, I examine the question of the independent LEC's market power in the local exchange and whether or not this results in the incentive or opportunity to engage in monopoly leveraging in interexchange telecommunications.

A. The Relevant Market is the Entire U.S. Interstate Telecommunications Market

Determination of market power includes both demand and supply responses to the firm's price change, including potential entry. A firm's ability to raise its price profitably depends on the extent to which the firm's customers reduce their purchases as a result, which is the own-price

---

[1] While practically every firm has some market power, due to market frictions such as transaction costs and transportation costs, empirical tests for market power generally specify some threshold level, such as a 5% or 10% increase over the competitive price. The empirical test also must make a determination of the estimated competitive price for the relevant market.

[2] See the discussion in FCC 95-427, In the Matter of Motion of AT&T Corp. to be Reclassified as a Non-Dominant Carrier, at 5.

elasticity of the firm's demand. The price responsiveness of the firm's demand depends in part on the substitutes available to the firm's customers. In addition, it depends on the reactions of the firm's competitors, as they alter their prices, product offerings, sales and marketing efforts, and amount of services sold. In addition, it is essential to take into account not only the supply response of the firm's existing competitors, but also the supply responses of new entrants that could be attracted to enter by the prospect of higher prices.

To evaluate market power, thus requires a definition of the firm's relevant product and geographic market. The product and geographic market definition should be sufficient to identify the demand and supply responses to the firm's pricing decisions. Excessively narrow definitions that overlook such responses would incorrectly overstate the firm's degree of market power and bias the relevant policy.

I agree with the present NPRM's tentative conclusion (¶ 119) that for the independent LECs, "all interstate, domestic, interexchange telecommunications services as the relevant product market." By this I mean that for a given customer the product market is a service that allows the customer to reach all other interstate, domestic, inter-exchange locations. I am not addressing distinctions between different ways in which the services are offered. I further agree with the tentative conclusion reached in the Interexchange NPRM (¶¶ 51-52) that the Commission should continue to treat "interstate, interexchange services as a single national market when examining whether a carrier or group of carriers acting together has market power." However, I do not agree with the present NPRM's tentative conclusion (¶ 126) that the Commission should "evaluate an independent LEC's point-to-point markets in which calls originate in its local exchange areas separately from its markets in which calls originate outside those areas, for the purpose of determining whether an independent LEC possesses market power in the provision of in-region, interstate, domestic, interexchange services." The Commission has consistently found interstate, domestic, interexchange services to be the relevant market for determining dominance. This was the standard applied to AT&T,[3] and any departure for the purposes of evaluating market power of the independent LECs in this market would be inconsistent and would bias the results. The Commission in its Fourth Report and Order defined a "single national relevant geographic market (including Alaska, Hawaii, Puerto Rico, U.S. Virgin Islands, and other U.S. offshore points) as the relevant geographic market, and applied the same standard to AT&T.[4] Again, any departure from this standard for the purpose of evaluating market power of the LECs in this market would be inconsistent and would bias the results, as well as being economically incorrect.

To summarize, the economically proper product market definition, for purposes of evaluating market power, should be all interstate, domestic, interexchange services and the geographic market definition should be national in scope. There are several determinative economic reasons for these conclusions.

All interstate, domestic, interexchange telecommunications services are the relevant product market because such services generally are sold together. A customer of an interexchange carrier purchases all domestic service to any location as one service, not a la carte. Services are not sold on a point-to-point basis, but rather, a customer is able to call all locations. Thus, such services almost always appear as a bundle, so that, unbundling them conceptually would depart from the way the services are both sold and purchased. As a consequence, companies compete by offering complete services and schedules of prices for the overall service. Customers usually choose a single carrier for their entire interexchange service rather than purchasing narrower product services from multiple carriers simultaneously. A market power test

[3] FCC 95-427, In the Matter of Motion of AT&T Corp. to be Reclassified as a Non-Dominant Carrier.

[4] FCC 95-427, at 9.

that failed to recognize the one-stop-shopping nature of interexchange services would be expected to yield incorrect results.

The geographic market definition should be national in scope because the major carriers, including AT&T, MCI and Sprint, compete nationally offering services that originate at all points and terminate at all points. Their service offerings are ubiquitous, not local or regional. Their facilities consist of national networks. Competition between these companies, therefore, takes the form of competition between national networks. Marketing and sales efforts of these companies are national in scope. Pricing programs and promotions are national as well. Limited geographic market definitions, such as "point-to-point" markets, are inappropriate. Services are not offered on such a point-to-point basis. To restrict the geographic market definition to anything less than a national definition (say a regional or local basis) would fail to account for the nature of the ubiquity, product offerings, pricing, facilities, and competition in this marketplace.

The LECs provide local exchange services that are regional or local in geographic scope. This does not imply in any way that their sale of long distance services departs from the national geographic market definition. Customers of the LECs can choose between the long distance services of national, regional or local providers of long distance services. The LECs ability to raise the price of telecommunications services will be constrained by the prices offered by the national carriers and any other carriers offering long distance services. To narrowly define markets by region or locality would misrepresent the extent of the competitive activities of the long distance carriers and thus present an inaccurate picture of the competitive alternatives available to the customers of the LECs. Thus, incorrectly narrowing the product or geographic market definition reduces the applicability of the market power test.

Geographic market definitions can sometimes be appropriate when transportation costs are significant. Transportation costs can limit customer choices in some types of markets, such as restaurants, when customers must travel to the firm's location. Transportation costs can also be a factor in some markets, such as cement, when firms transport their products and transportation costs are a significant share of the market value of the good. These considerations may apply to some extent in long distance telecommunications. There are costs to providing a point of presence for long distance carriers. However, these costs already have been incurred by the national carriers, in most locations. Therefore, at those locations, service is almost universally available and customer transportation costs are not an issue, since customers have access to all carriers through their local exchange, through competitive access providers, or other access providers such as wireless companies. There is no problem of travelling to reach a firm that is "far away." All carriers that serve the area are available at the customers location, the local transport costs of the carriers do not differ greatly.

Therefore, the pricing of interexchange services of the independent LECs is constrained by competition from national, regional and local providers of interexchange services. The pricing of interexchange services is constrained by competitive product offerings that consist of interstate, domestic, interexchange telecommunications services. Moreover, the services offered by the independent LECs compete with services provided by carriers that operate in the national market for interstate, interexchange services.

B. Market Share in Interexchange Telecommunications

Having established the definitions of the product and geographic markets, is apparent that the market shares of the independent LECs in interexchange telecommunications are very small. Market shares alone do not determine market power. Thus, even a high market share in an industry with low barriers to entry, opportunities for product differentiation, or ongoing technological change, does not necessarily confer market power. The firm's market share does not yield market power because entrants can take away customers with lower prices, differentiated products, or product innovations. However, while a high market share is not sufficient to indicate market power, a market share that is very low or even negligible is sufficient to indicate the absence of market power.

Table 1 lists the market shares of the interexchange long distance carriers as of the first quarter of 1996. The four largest national carriers (AT&T, MCI, Sprint, and LDDS Worldcom) have over 85% of the market. Market shares of other individual companies drop off dramatically. Next, for example, is Frontier Companies with a 1.9% market share and Cable and Wireless Communications, Inc. with a 1% market share, while all other companies have shares *below 1% of the market.* These minuscule shares cannot be consistent with a "dominant carrier" classification. Moreover, if the largest carrier, AT&T Communications, is nondominant with 53% of the market, surely smaller carriers, including the independent LECs with market shares less than one hundredth those of AT&T, cannot be classified as dominant. This much is a matter of common sense.

TABLE 1
INTEREXCHANGE LONG DISTANCE CARRIERS MARKET SHARES
(BASED ON 1995 TOTAL TOLL SERVICE REVENUES)

Firm	Market Share
AT&T Communications, Inc.	53.0%
MCI Telecommunications Corp.	17.8%
Sprint Communications Co.	10.0%
LDDS Worldcom	5.0%
Frontier Companies, et al.	1.9%
Cable & Wireless Communications, Inc.	1.0%
LCI International Telecom Corp.	0.9%
Excel Telecommunications, Inc.	0.5%
Telco Communications Group, Inc.	0.3%
Midcom Communications, Inc.	0.3%
Tel-Save, Inc.	0.2%
U.S. Long Distance, Inc.	0.2%
Vartec Telecom, Inc.	0.2%
GE Capital Communications Services Corp.	0.2%
General Communication, Inc.	0.2%
MFS Intelnet, Inc.	0.2%
Business Telcom, Inc.	0.2%
Communications Telesystems, Int'l.	0.2%
Oncor Communications, Inc.	0.2%
The First Group, Inc.	0.2%
American Network Exchange, Inc.	0.1%
Others	7.3%

Source: Federal Communications Commission, *Long Distance Market Shares, First Quarter 1996*, Table 5 (July 1996).

Another measure of market share is presubscribed lines. Lines are said to be presubscribed to the long distance carrier that receives ordinary telephone calls placed on the line.[5] According to the FCC citing NECA, as of December 1995, of the 153 million presubscribed lines, the shares were 66% for AT&T, 16% for MCI, 6% for Sprint, and 3% for LDDS, for a combined total of 91%.[6] These carriers are not classified as dominant. No remaining carrier, can conceivably be classified as dominant.

Any reasonable projected expansion of market share by the independent LECs cannot be expected to change this situation. The market shares of individual independent LECs in long distance can be expected to remain negligible in comparison with the IXCs.

C. Supply and Demand Elasticities in Interexchange Telecommunications

1. Supply Elasticity in Interexchange Telecommunications

In its classification of AT&T as nondominant, the Commission declared that "in the interstate, domestic, interexchange market, supply is sufficiently elastic to constrain AT&T's unilateral pricing decisions."[7] AT&T, cited in the Order, stated that in 1993 there were more than 500 carriers providing service in the United states, 394 of which provided equal access service in at least one state, nine carriers provided equal access and service at least 45 states, 81 regional carriers served at least four states, and at least twelve interexchange carriers served every state.[8] As the Commission states, "AT&T asserts, and no one disputes, that MCI and Sprint alone can absorb overnight as much as fifteen percent of AT&T's total 1993 switched demand at no incremental capacity cost; that within 90 days MCI, Sprint and LDDS/Wiltel, using their existing

---

[5] Industry Analysis Division, Common Carrier Bureau, Federal Communications Commission, July, 1996, *Long Distance Market Shares*, First Quarter, 1996, at 3.

[6] *Id.*

[7] FCC 95-427, at 16.

[8] FCC 95-427, at 14.

equipment, could absorb almost one-third of AT&T's total switched capacity; or that within twelve months, AT&T's largest competitors could absorb almost two-thirds of AT&T's total switched traffic for a combined investment of $660 million.[9] The FCC concludes that "AT&T's competitors have sufficient excess capacity to constrain AT&T's pricing policies." Such constraints apply with even greater force to the independent LECs.

The market supply elasticity applies to all carriers in the interexchange market. This argument carries over to all carriers in the market. It pertains with particular strength to the independent LECs since a minor capacity adjustment for the large interexchange carriers (AT&T, MCI, Sprint) is sufficient to constrain any of the independent LECs.

Resale is an important component of supply elasticity in long distance services. Reseller purchases from long distance carriers comprise over $4.9 billion of revenue from wholesale minutes in 1994. The resellers sales represent over $11.6 billion of total switched services in 1995.[10] There are over 1,000 companies that resell telecommunications services. Many of these companies are switchless resellers, that is, they do not own their own switching facilities or lines, and make retail sales by making volume wholesale purchases from major facilities-based carriers.[11]

---

[9] FCC 95-427, at 16-17.

[10] This is according to the Telecommunications Resellers Association, (internet page www.tra-dc.org), which represents over 400 companies involved in the switchless resale of long distance services.

[11] *Id.*

2. Demand Elasticity in Interexchange Telecommunications

The FCC found further that "residential customers are highly demand-elastic and will switch to or from AT&T in order to obtain price reductions and desired features." Citing AT&T data showing that as many as twenty percent of its residential customers change interexchange carriers at least once a year, the FCC concluded that the "high churn rate among residential consumers -- approximately 30 million changes are expected in 1995 -- demonstrates that these customers find the services provided by AT&T and its competitors to be very close substitutes."[12] In addition, the FCC found that business customers also are "highly demand elastic."[13] They reaffirm their earlier finding that "business users consider the offerings of AT&T's competitors to be similar in quality to AT&T's offerings."

The FCC allows for the possibility that AT&T may have goodwill and brand recognition in the marketplace that distinguish its offerings from those of its competitors, making its demand less elastic that those of its competitors. Thus, if anything AT&T's goodwill, brand recognition, and marketing expenditures mean that the demand elasticity of its actual and potential competitors is higher than that of AT&T. If, as the FCC asserts, AT&T's demand is sufficiently elastic for it to lack market power, then its actual and potential competitors with less goodwill, brand recognition, or marketing expenditures, must also lack market power. Even if AT&T were to have market power, the offerings of competitors with less goodwill, brand recognition, or marketing expenditures would have less, if any, market power.

---

[12] FCC 95-427, at 17.

[13] FCC 95-427, at 18.

When services are close substitutes, market demand cannot be highly elastic for some firms and inelastic for others. Put simply, all firms in this market face approximately the same demand elasticity when their products are comparable. Thus, independent LECs, *no matter their market share or size*, face basically the same elasticity of demand as the interexchange carriers. If the elasticity of residential and business demand is sufficient for the conclusion that the interexchange carriers do not posses market power, it is also sufficient to imply that none of the independent LECs possess any market power.

D. Cost Structure, Size and Resources

The cost structure, size and resources of the independent LECs indicate that they are non-dominant. While these carriers may have a large share of the local exchange market, their operating revenues and investment in facilities are small in size in comparison with the interexchange carriers. Table 2 shows the revenue, plant investment and presubscribed lines of AT&T, MCI, and Sprint in 1994. I use 1994 data to compare with related data for the same year collected for over 457 of the independent LECs. To give a complete summary of the data for such a large number of firms, I present the data as a frequency distribution.

Table 2
INTEREXCHANGE CARRIERS
(1994)

Company	Revenue ($ Millions)	Plant Investment ($ Millions)	Presubscribed Lines
AT&T Communications, Inc.	$37,166	$26,537	103,957,425
MCI Telecommunications Corp.	$11,715	$8,875	22,040,062
Sprint Communications Co.	$6,805	$3,554	9,467,999
LDDS WorldCom	$2,221	$944	1,954,198

Sources: Revenue and Plant Investment from FCC, *FCC-State Link BBS*, table entitled "Toll Carriers with Over $100 Million in 1995 Revenue". Presubscribed Lines from FCC, *Long Distance Market Shares First Quarter 1996*, table 4.

Table 3 presents the operating revenues in 1994 for the independent LECs, the RBOCs, and the three major IXCs (AT&T, MCI, and Sprint). The ILEC's distribution has a mean of approximately $62 million which is clearly minuscule in comparison with the three major interstate carriers. For example, AT&T which was declared to be nondominant has operating revenues of over $37,166 million. GTE, the largest of the ILECs, has operating revenues of $12,842 million, which is well below that of AT&T. Thus, the size of the independent LECs is generally small enough so that one cannot conclude that they have market power in long distance telecommunications. Revenues provide some indication of the size of the firm. Whatever information is provided by size, it is clear that none of the independent LECs are dominant carriers. Of course, small companies can grow and become successful in the future. However, the disproportion in size is sufficient to conclude that the independent LECs are not dominant nor